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IN THE

Supreme Court of the United States

OCTOBER TERM, 1971

No. 71-1059

KERN COUNTY LAND COMPANY,
Petitioner,

v.

OCCIDENTAL PETROLEUM CORPORATION,
Respondent.

PETITIONER'S REPLY TO RESPONDENT'S BRIEF IN OPPOSITION

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Petitioner Kern County Land Company ("New Kern") respectfully submits this brief in reply to the brief of respondent Occidental Petroleum Corporation ("Occidental") in opposition to the grant of a writ of certiorari.

The Option Issue

Occidental's answering brief begs the question presented with respect to the Occidental option by proceeding on the assumption that options are "transactions other than purchases and sales" (Br., p. 20). In fact, the court of appeals in its opinion below expressly recognized that Section 3(a)(14) of the Securities Exchange Act defines "sale" to include any "contract to sell" and that an option is "a con-

tract to sell in a dictionary sense." Nevertheless, the court held it to be the rule "in this circuit" that the sale of an option "is not a sale for purposes of § 16(b); this occurs only when [and if] the optionee exercises the option" (Opinion Below, 13A).

In ignoring the statutory definition of the term "sale," the court did not discuss the possibility of speculative abuse inherent in an insider's sale of an option. In a conflicting decision, the Court of Appeals for the Seventh Circuit found Section 16(b) liability on virtually identical facts, expressly holding that "[t]he insider's sale of options in his stock is well adapted to speculation and abuse of inside information, *whether or not the option is subsequently exercised*" and that "[s]ale of such purchase rights provides an easy vehicle for the use of inside information in extracting profits from the stock itself" (*Bershad* v. *McDonough*, 428 F.2d 693, 698 (7th Cir. 1970), *cert. denied*, 400 U.S. 992 (1971). (emphasis added)*

Occidental's argument in answer to the foregoing is that the sale of an option does not confer a "sure-thing profit" because unanticipated events, such as the bottom falling out of the market, might in retrospect make the sale of the option unprofitable (Br., p. 20). The notion that Section 16(b) liability may be imposed only if there is 100% assurance of profit flies in the face of the express statutory

* While conceding the possibility that some options may be "in truth and fact a sale" and thus within Section 16(b), Occidental disputes that this was such an option. In so doing, Occidental relies either upon its own version of the facts (as in the case of the economic reasonableness of the option price) or in many instances upon facts dehors the record (as in its explanation of the proxy which it gave its attorney). For reasons discussed in the Petition for Certiorari (pp. 13-15), we respectfully submit that if the question of whether an option is a "sale" for Section 16(b) purposes must turn on the factual question of whether or not it is a disguised sale summary judgment for defendant, as the court of appeals directed, was erroneous.

purpose of "preventing the unfair use of information" obtained by insiders. An insider is conclusively presumed to have access to inside information not available to other stockholders. In entering into transactions in his company's securities, including the sale of an option, his access to inside information gives him an *opportunity* to profit not enjoyed by other stockholders. The possibility that the insider's speculation may on rare occasion boomerang and prove unprofitable is no reason for permitting him to keep the fruits of his speculation in the overwhelming number of instances where, as is to be expected, it proves to be profitable.

So here, despite Occidental's contention that the option did not give it a "sure-thing profit," less than one month after becoming a 20% beneficial owner it did receive over $8,000,000 cash in hand in return for the option itself, and the likelihood of the option being exercised, as it was at a profit to Occidental of over $17 million, far outweighed the possibility of non-exercise or of any loss to Occidental, if indeed it existed. Certainly, Occidental's President, Dr. Hammer, does not appear to have had the possibility of any loss in mind, when shortly after entering into the option agreement he boasted to Fortune Magazine of looking forward to a profit of over $17 million, which he aptly observed "isn't bad for two weeks' work."

The Exchange Issue

Occidental's answering brief attempts to minimize the importance of the question of whether or not the exchange of Old Kern shares for Tenneco preference stock constitutes a "sale" of Occidental's Old Kern shares by arguing this case "reflects conditions and responses that prevailed during the merger activity of the mid-1960's" (Br., p. 27). While it may be that market conditions in recent months

have led to a decline in the number of takeover attempts that were previously reported, there is no reason to believe that such activity will not increase as the market improves and that the exchange of shares of one company for those of another will not continue to occur with significant frequency.

Moreover, as pointed out in the Petition for Certiorari (p. 19, *et seq.*), the decision below is not confined, as Occidental's brief maintains, to exchanges of stock following upon an unsuccessful tender offer, but suggests that *ad hoc* exemptions from 16(b) may be granted whenever the court feels that a Section 16(b) recovery would be "repugnant" to its "sense of equity" (Opinion Below, 13A), in spite of what this Court has recently described as the "mechanical quality" of the statute. *Emerson Electric Co.* v. *Reliance Electric Co.*, U.S. (1972) (Slip Op., p. 7).

Indeed, Occidental's answering brief concedes that the test of Section 16(b) liability applied by the court of appeals here was one which "requires a careful examination of the facts . . . on a case-by-case basis" and that "[a] decision on the facts of this case cannot resolve future merger cases, . . ." (Br., p. 22). Such an *ad hoc* approach represents a drastic repudiation of the uniform line of authority* which has held, until now, that the courts will not concern themselves with the "details of transactions" but only with the question of whether or not a particular *type* of transaction "objectivity defined" might serve as a vehicle for speculative abuse. *Emerson Electric Co.* v. *Reliance Electric Co.*, *supra*, (Slip Op. p. 7n). Thus, for example, in the leading case of *Blau* v. *Lamb* (*supra* fn.), the court objectively defined the question to be decided as "whether a conversion of preferred stock into common constitutes a Section 16(b) 'sale'" and expressly rejected as irrelevant con-

* E.g., *Blau* v. *Lamb*, 363 F.2d 507 (2d Cir. 1966) *cert. denied*, 385 U.S. 1002 (1967); *Newmark* v. *RKO General, Inc.*, 425 F.2d 348 (2d Cir.) *cert. denied*, 400 U.S. 854 (1970).

sideration of the control position of the defendant insider. 363 F.2d 517, 520-21.

The new approach of the court of appeals, which focuses upon the particularized facts rather than the type of transaction involved, necessarily undermines the "mechanical quality" of the statute, which Congress intended, and encourages defendants not only to enter into short-swing transactions but also when sued, to litigate Section 16(b) actions in the hope that they too will be the beneficiaries of an *ad hoc* exemption granted upon a "case-by-case basis."

CONCLUSION

For the reasons set forth above and in the Petition for Certiorari, it is respectfully submitted that a writ of certiorari be granted and the judgment of the Court of Appeals for the Second Circuit reversed.

Respectfully submitted,

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